No. 17954

United States Court of Appeals

FOR THE NINTH CIRCUIT

SHERWOOD & ROBERTS-KENNEWICK, INC., a Washington corporation,
Appellant,

vs.

ST. PAUL FIRE & MARINE INSURANCE COMPANY, a Minnesota corporation,
Appellee.

No. 17954

APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF WASHINGTON
SOUTHERN DIVISION

BRIEF OF APPELLEE

FRED C. PALMER
Of Palmer, Willis & McArdle
506 Miller Building
Yakima, Washington
Attorney for Appellee

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PRELIMINARY STATEMENT

This appeal involves a review of an action tried before United States District Judge William T. Beeks sitting with a jury at Yakima, being in the Eastern District of Washington, Southern Division. As indicated by appellant, jurisdiction is based upon diversity of citizenship, the plaintiff-appellant being a Washington corporation and the defendant-appellee being a Minnesota corporation.

Appellee will adopt the designation set forth in appellant's brief and hereafter plaintiff-appellant will be referred to as "S. & R." and the appellee will be designated as "St. Paul".

This action arises out of a "Mortgage bankers blanket bond" issued to S. & R. by St. Paul in the blanket sum of $250,000.00. Covered under the bond by St. Paul are the employees of some seventeen corporations, all being subsidiaries or under the general supervision of the home office in Walla Walla, Washington, being Sherwood & Roberts, Inc. Claims were made by S. & R. against four employee-principals under the bond, being Robert D. Chamberlin, Dean Dion, John Koster and Kermit Krueger.

Trial of the action commenced on November 20, 1961, and was concluded upon December 12, 1961, with the jury finding in favor of St. Paul as to St. Paul's liability under the bond.

Under the pretrial order the parties had stipulated that only the issue of liability of St. Paul under its bond would be submitted to the jury, with the question of damages, if the jury found liability, being reserved for determination at a later trial. (R. 46) The question of liability was submitted to the jury in the form of interrogatories. The interrogatories covered the "Walker transactions" and the "Williams transactions". A general interrogatory was asked in relation to each of the above transactions with the jury being instructed that in the event they found fraud or dishonesty, in any connection with reference to either of said transactions, they were then required to answer separately a series of interrogatories concerning the fraudulent transaction. Since the jury answered the general questions on each transaction in the negative, it was not necessary for them to further consider the individual questions under each transaction. (R. 129-132)

COUNTER-STATEMENT OF THE CASE

Appellant in many instances in its statement of the case presents to the court only the evidence most favorable to the appellant's contentions. For this reason appellee feels required to set forth the evidence most favorable to the appellee and upon which the jury based its verdict in favor of the appellee.

(1)

THE WALKER TRANSACTIONS

In considering all phases of the various loans made to

the Walker Companies and Palmer Walker personally, consideration should first be given to the importance of the income to S. & R. received from the Walker Companies. During the period of time of 1953 to 1959 Walker Motors - Kennewick paid off loans to S. & R. in the total amount of $1,606,000.00. Walker Motors - Union Gap between the periods 1955 and 1959 paid off a total of $648,-428.00; Tri-City Rambler and European Motors during the period 1957-1959 paid off principal loans of $66,-098.00; Palmer Walker personally during all of these periods paid off a total sum of $37,300.00. The total of loans paid off by Palmer Walker personally and by his companies is the sum of $2,357,826.00 during the period of 1953 to 1959. The total interest charged and received by S. & R. upon these loans is the sum of $48, 187.00 (Last Page Defendant's Exhibit A-19) The Exhibit referred to is a report from W. G. Strong, treasurer of S. & R. Inc., the parent corporation in Walla Walla, to Donald Sherwood, the president, dated February 15, 1960. During the period 1956 to 1959, S. & R. received from consumer contracts purchased from Walker Companies, discounts in the total amount of $88,615.96. This represented 22.9% of the total discounts to be received by S. & R. from all sources on consumer contracts. (Defendant's Exhibit A-28) The total gross income received by S. & R. from either direct loans to Walker Companies and Palmer Walker or from consumer paper

generated by the Walker Companies and sold to S. & R. is the sum of $136,802.96.

(2)

THE LOANS MADE TO WALKER COMPANIES

On April 15, 1957, Robert D. Chamberlin on behalf of S. & R. made a loan to Walker Motors - Union Gap in the sum of $5,550.00. This loan was evidenced by a note and the note was secured by the assignment of another note executed by Walker Motors - Union Gap to Palmer Walker, individually. On July 31, 1959, the unpaid balance upon this loan was the sum of $3,107.36. (R. 20-21)

On November 19, 1958, Chamberlin on behalf of S. & R. made flooring loans on radios and boats to Walker Motors of Kennewick and to Palmer Walker d/b/a Walker Enterprises. These two loans were actually made before the above date and were evidenced by separate notes but upon November 19, 1958, they were consolidated in the sum of $13,974.34. In addition to the security of radios and boats, the consolidated loan was personally guaranteed by Palmer Walker. The balance due on July 31, 1959, on this loan was $9,360.87. (R. 21, Plaintiff's Exh. 61, R. Vol. 9, p. 2003-2004) This loan appeared, as did all loans on the monthly finance loan register forwarded to Walla Walla (Defendant's Ex. A-10)

Between December 26, 1957, and November 19, 1958, Robert D. Chamberlin, or employees acting under his di-

rection, on behalf of S. & R. made flooring loans to Walker Motors - Kennewick, each loan being evidenced by a note, which note was secured by chattel mortgage on certain motor vehicles. On November 19, 1958, there remained unpaid on these various loans the sum of $20,218.20. (R. 21) Between May 28, 1957, and January 14, 1958, Robert D. Chamberlin or employees acting on behalf of S. & R., made flooring loans to European Motors Inc. covering motor vehicles and secured by chattel mortgages on said motor vehicles, and on November 19, 1958, there remained due on said loans the sum of $12,371.95 (R. 22). About a month or six weeks prior to November 19, 1958, Dean Dion, an employee of S. & R., working under Mr. Chamberlin, reported to Chamberlin that it appeared various vehicles floored on both loans had been sold without S. & R. being paid. Dion thereafter verified it and spoke to Walker in regards to pay-off but was unsuccessful in getting the money and so reported to Chamberlin. Chamberlin then contacted Walker and asked him point-blank what the situation was and whether or not he had sold vehicles "out of trust". Walker told Chamberlin that vehicles had been sold without being paid for. Dion and Chamberlin then discussed the problem and had some differences of opinion as to how to handle it. Dion's first impulse was to call the account but Chamberlin determined to analyze the situation, and consider the previous experience with Walker and the caliber of paper he had been generating

for them on consumer contracts. Chamberlin met with Walker and explained the situation, including the alternatives. Walker was very disturbed about the situation and told Chamberlin that the decision was his. Walker further advised Chamberlin that his business manager, Mr. Bishop, had handled the transactions during this time and that he had relieved Bishop of his responsibilities. Chamberlin then determined in his business judgment to collateralize both of these loans and continue doing business with Walker. (R. Vol. 9, pp. 2005-2007) Both of these loans were then rewritten, the Walker Motor Co. - Kennewick loan being in the amount of $20,218.20 and being secured by shop equipment, parts, inventory and leasehold improvements, together with Walker's personal guaranty. The European Motors Inc. loan was rewritten in the amount of $12,371.95 and likewise secured by equipment, tools, parts inventory and leasehold improvements on that business together with Palmer Walker's personal guaranty. (Plaintiff's Exhibit 61, R Vol. 9, p. 2007)

On July 31, 1959, the balance due on the loan to Walker Motors - Kennewick was the sum of $19,254.05. On the same date the balance due on the European Motors Inc. loan was the sum of $11,854.63 (R. 21-22).

On December 8, 1958, Chamberlin on behalf of S. & R. loaned Palmer Walker personally the sum of $15,000.00 which was evidenced by a note signed by Walker

and his wife. This loan was made for the purpose of enabling Walker to purchase parts, equipment and miscellaneous items in connection with Walker's acquiring the Rambler franchise from American Motors. (R. Vol. 5, pp. 1037-1038) On January 15, 1959, the sum of $11,000.00 was paid back to S. & R. on this loan and upon July 31, 1959, the balance due on this loan was the sum of $4,-140.00. (R. 22)

All of the above loans appeared on the monthly finance loan register for November, 1958, and December, 1958, forwarded in the regular course of business to Sherwood & Roberts, Inc., Walla Walla. (Defendant's Ex. A-10) All loans made by S. & R. and pursuant to the regular business routine maintained by Robert D. Chamberlin as manager appeared on the loan register. (R. Vol. 4, pages 843-853; 896-898) No one in executive authority in Sherwood & Roberts Inc. in Walla Walla looked over the monthly finance loan registers to see what large loans were being processed at the branches, however. (R. Vol. 5, p 1224)

In connection with these various loans it should be considered that Mr. Donald Sherwood, President of S. & R., did not provide the S. & R. employees with a manual of procedure as he did not believe in them. (R. Vol. 5, p 1224) Another important consideration is the fact that all Sherwood & Roberts branch organizations are de-central-

ized and managers, such as Robert D. Chamberlin, were completely self-sufficient. Each manager is in complete authority as to the area he serves. (R. Vol. 5, pp. 1128-1129, testimony of Donald Sherwood)

(3)

THE RAMBLER FRANCHISE NEGOTIATIONS

During the latter part of 1958, Palmer Walker determined that it was necessary to secure a better selling car for European Motors to handle. He made this determination in view of the fact that European Motors had been losing money and had discussions with the district manager for American Motors preliminary to securing the franchise. (R. Vol. 5, pp. 1032-1033) On or about December 15th or 16th, 1958, Walker called Chamberlin, advising him that a field representative of American Motors was going to be in town and that they were working on the Rambler Franchise. This was already known to Chamberlin. Walker requested that Chamberlin have lunch with the American Motors representative, Mr. Townsend, for the purpose of discussing the new Rambler location and Walker's application for the franchise. At the luncheon meeting Chamberlin told Townsend of American Motors of the advisability of locating the Rambler franchise in Kennewick, and further advised Townsend that S. & R. were doing business with Walker and were prepared to handle the volume of Ramblers as to flooring. Chamberlin was then asked to write a letter to American Motors and

did write the letter of December 17, 1958 (Pl. Ex. 68). Chamberlin in this letter committed S. & R. to a flooring line of $100,000.00 in anticipation of the Rambler franchise being granted and also made personal comments about their previous experience with Walker. This meeting was held approximately a month after the consolidation and collateralizing of the loans of November 19, 1958. Chamberlin at that time regarded his relationships with Walker as being excellent and the previous problems of November, 1958, were a closed book, having been collateralized by a capital loan. S. & R.'s experience as far as repossessions on cars sold by Walker, and financed through S. & R. had been excellent, there being only two Volkswagens repossessed during their entire experience with Walker. (R. Vol. 4, p. 827) Chamberlin had no knowledge of the financial statement of European Motors that was mailed to American Motors by Palmer Walker. Chamberlin did not see this financial statement prior to the trial. (R. Vol. 9, p. 2014) After making the commitment to American Motors, Chamberlin on December 30th, 1958, forwarded to American Motors, wholesale drafting instructions for the Tri-City Rambler Inc., which was the new name of European Motors. Problems developed, however, as far as the drafting instructions were concerned because S. & R. was not a nationally recognized finance organization and for that reason were not acceptable to American Motors.

Chamberlin called Donald Sherwood to discuss the problem and then made a trip to Walla Walla with the drafting instructions and the franchise agreement. At no time did he have the financial statement introduced in evidence, (Plaintiff's Ex. 68-a) which statement was secured from the files of American Motors shortly before trial. (R. Vol. 4, p. 963) Shortly after this meeting with Sherwood in Walla Walla, Chamberlin talked to Mr. Stricker of the Seattle First National Bank in Richland and the Seattle First National Bank agreed to honor the drafts of American Motors on Ramblers shipped to Tri-City Rambler Inc., provided S. & R. would enter into hold-harmless agreement. Chamberlin then called Donald Sherwood, advising him of the solution to the matter of drafting that Chamberlin had worked out and Sherwood granted Chamberlin the authority to sign the letter of guarantee. The flooring commitment to Tri-City Rambler Inc. had been previously made on December 17, 1958 and in Chamberlin's discussion with Donald Sherwood he did not ask for flooring authority as it was, of course, evident that the commitment had been made in the letter. (R. Vol. 9, pp. 2010-2018)

(4)

EXCHANGE OF CHECKS BETWEEN WALKER MOTORS - KENNEWICK AND S. & R.

Dennis C. Hayden was the accountant for all of S. & R.'s Pasco, Kennewick and Richland offices. His duties

were to handle all accounting procedures, including reporting of all the Tri-City offices, and making certain that the bookkeeping procedures were proper. A daily cash report was prepared by all of the Tri-City Branch offices, reflecting receipts, disbursements, and cash in bank; which was forwarded daily to Walla Walla. (R. Vol. 7, pp. 1651-1652)

The daily cash report forwarded to Walla Walla showed a book overdraft situation daily, particularly during the period of the fall of 1958, through the spring of 1959. Chamberlin was experiencing difficulty in getting enough funds to take care of the volume of business committed in the Tri-City area and further demands were being made upon him by Walla Walla to return funds. (R. Vol. 9, pp. 2018-2019) Because of the overdraft situation on the books of S. & R., together with the further fact that at the month end the books could not be closed unless they were in the black, the trading of checks with Walker Motors-Kennewick was temporarily instituted. While this perhaps was an unusual accounting procedure, it did not result in any loss whatsoever to S. & R. (R. 7, pp. 1657-1658, Dennis C. Hayden)

Although Bert Edwards of the executive committee in Walla Walla knew of this overdraft situation on the books of S. & R., and advised Chamberlain to stop it, Donald Sherwood, President of the Company, tacitly approved the practice as long as Chamberlain did not get

caught in a bank overdraft situation. Chamberlin testified to this conversation as follows:

> "A. I did not take it up with him. He called me and related that he was conscious of what was—what the situation was, wanted to put me on notice that a book overdraft was one thing. However, if the book overdraft resulted in a bank overdraft, that I would be, in his terms, and I quote, 'standing alone' ".

(R. Vol. 9, pp. 2019-2020)

This testimony of Robert Chamberlin was never refuted on rebuttal by Donald Sherwood. Whenever an exchange of checks was made, no notes were marked "Paid" or chattel mortgages satisfied, thus the security remained the same. Each check transaction balanced the other out (R. Vol 6, pp. 1397-1398, testimony W. G. Strong).

(5)

CONSOLIDATION OF LOANS ON JULY 31, 1959, IN THE AMOUNT OF $47,716.91

The parent corporation of Sherwood & Roberts in Walla Walla was advised of the fact that the Walker Companies in Kennewick had sold cars "Out of trust" by Dean Dion. W. G. Strong, treasurer of the Walla Walla corporation, during a visit to Kennewick in the early part of 1959, had a conversation with Dean Dion during which conversation Dion not only told Strong that they had problems with Palmer Walker but also that they had some

cars out of trust in 1958 and that Walker owed them considerable money. (R. Vol. 9, pp. 1971-1972) From November 19, 1958, to the fall or late fall of 1959, there were no "out of trust" transactions by Walker. (R. Vol. 9, p. 2022)

During the late spring of 1959 S. & R. in the Tri-City Area was in an extremely tight money situation. Chamberlin was requesting funds from Walla Walla but only receiving a limited amount, it not being enough to take care of their business committments. Likewise, it was not possible to forward funds to Walla Walla, as was being demanded. Chamberlin discussed the situation with Strong, advising him that if they could not get funds, then the only other alternative was to get rid of some of their dealers. Strong agreed that it would be advisable to get rid of Walker Motor-Kennewick as a flooring account because of the heavy demand by Walker for Volkswagen flooring. Chamberlin saw Walker and requested that he seek other financing for this corporation, as S. & R. could no longer carry the volume of business that Walker was producing. (R. Vol. 9, pp. 2022-2026)

Chamberlin made a determination as to the assets of Tri-City Rambler Inc. available to secure the loan. He determined that the total valuation of all security was $61,313.25 which includede Palmer Walker's personal guarantee in the sum of $15,000.00. (R. Vol. 9, pp. 2027-2028) Contained in Pls. Exhibit 58, which is the S. & R.

file on this loan, is a letter dated August 3, 1959, from Chamberlin to Iver Turnquist, an employee in the S. & R. office. In this letter Chamberlin directed Turnquist to close the loan and on the chattel mortgage from Tri-City Rambler Inc., all physical assets of the corporation were to be listed, together with accounts receivable and the assignment of reserves then accrued in the S. & R. office and all that would accrue in the future to Walker Motors-Kennewick, Walker Motors-Union Gap and Tri-City Rambler Inc.

Pursuant to these directions, Turnquist consolidated the five previous loans discussed *supra* in their then unpaid balances, which totalled $47,716.91. A note was prepared, signed by Tri-City Rambler Inc., through their corporate officers with a personal guarantee by Palmer Walker for the first $15,000.00, all with interest at the usual 12% charged by S. & R. Attached to the letter to Turnquist was a check presumably from Walker in the amount of $1102.83 covering interest to date on the loans being consolidated. This loan was reported in the routine manner on the monthly loan register, dated August 20, 1959, and forwarded to Walla Walla. (Page 3, Defendant's Exhibit A-10)

Chamberlin had no knowledge that Tri-City Rambler Inc. was losing money between November 30, 1958, through July of 1959. (R. Vol. 9, 2120) The situation on Tri-City Rambler Inc.'s loss position was not brought out

until the certified audits were made in June and July of 1960. As a result of S. & R. being relieved of flooring commitments to Walker Motors-Kennewick by reason of the loan consolidation and its assumption by Tri-City Rambler Inc., Chamberlin was able to return to the Walla Walla office from S. & R. in Kennewick during the next 90 days, approximately $125,000.00. The daily cash report also returned to the black. (R. Vol. 9, p. 2033 and R. Vol. 7, p. 1653)

The chattel mortgage securing the loan above discussed was re-filed the latter part of September or October 1959 due to the fact that the chattel mortgage originally taken was not filed within the statutory ten day period. (R. Vol. 4, pp. 833-834) This is mentioned on page 22 of appellant's brief but no significance attaches to this re-filing.

(6)

SITUATION ON FLOOR CHECKING RAMBLERS IN THE FALL OF 1959 AT TRI-CITY RAMBLER, INC.

On page 22 of appellant's brief, testimony is referred to indicating that cars were out of trust in the fall of 1959, which was reported to Chamberlin by Dennis Englund and Dean Dion. At this time S. & R. was not flooring any Volkswagens, as the July 31, 1959 loan consolidation had eliminated Volkswagen flooring. Ramblers were, of course, being floored for Tri-City Rambler, Inc. While

it is true certain Rambler automobiles were not present at the time Dennis Englund made floor checks in the fall of 1959, this situation was brought about by an error on the part of American Motor Company shipping cars without invoices and sending invoices without shipping cars. This made it very difficult to determine whether or not cars were actually missing, and for a period of sixty days the true picture was not evident. (R. Vol. 4, pp. 877-878, Denny Englund; R. Vol. 9, pp. 2033-2034, Robert Chamberlin; R. Vol. 5, pp. 1121-1122, Palmer Walker)

When this matter was reported to Chamberlin, he checked it out and discovered the mixed-up shipping situation at American Motors. As a consequence Chamberlin took no action at this time.

(7)

TEMPORARY FLOORING OF VOLKSWAGENS IN DECEMBER, 1959

In December of 1959 Palmer Walker told Chamberlin that the National Bank of Commerce in Kennewick had refused to furnish funds so that Walker Motors Kennewick could pay for a boat-load of Volkswagens; that the National Bank of Commerce had requested Walker to pass this particular boat-load. Walker wanted S. & R. to floor this load and discussed it with Chamberlin. Chamberlin told Walker that they had previously agreed that the Volkswagen corporations were no longer to be floored by

S. & R. and that he could not grant a dealer agreement to Walker on the Volkswagens. Chamberlin did, however, make a commitment to floor one boat-load of Volkswagens so that it would not have to be passed. (R. Vol. 9, pp. 2034-2036)

These flooring loans were made on January 6, 1960 and appeared on the January finance loan register. (Defendant's Exhibit A-10, p. 4)

Early in January, 1960, Chamberlin called Donald Sherwood and related to him his conversation with Walker. Chamberlin requested that the Volkswagen flooring be returned to S. & R. Sherwood stated in effect to Chamberlin that since they had gotten rid of them last summer he didn't think they should handle them now. Chamberlin then told him that he had committed for one boat-load of Volkswagens and had floored them. Sherwood then told Chamberlin not to floor any more until they could look the situation over. (R. Vol. 9, p. 2037) Chamberlin at the time of the temporary flooring had no definite knowledge of Walker corporations selling cars "out of trust" since the fall of 1958.

(8)

W. G. STRONG REPORT TO DONALD SHERWOOD ON WALKER MOTORS OF FEBRUARY 15, 1960

Appellant has emphasized that the Strong report was prepared primarily from information and figures furnished

Strong by Chamberlin. Some enmity existed upon Chamberlin's part toward Strong which was based upon a statement made to Chamberlin by Bert Edwards of the executive committee in Walla Walla. In the fall of 1959 while Chamberlin and Edwards were in Seattle on S. & R. business, Edwards told Chamberlin in commenting about a lawsuit that had been commenced against S. & R. in Kennewick, that Strong appeared to be pleased about the lawsuits as he had his guns trained on Chamberlin. Edwards further told Chamberlin that he thought this might be significant. (R. Vol. 7, pp. 1610-1612) The above statement to Chamberlin by Edwards explains Chamberlin's instructions to Dion not to give any information to Strong.

On February 15, 1960, W. G. Strong prepared a report to Donald Sherwood on all Walker companies. (Defendant's Exhibit A-19). The preparation of this report was initated by Chamberlin's conversation with Don Sherwood requesting Sherwood to reconsider the Volkswagen flooring account. Sherwood requested that Chamberlin get together with Strong and give him a report. (R. Vol. 9, p. 2038) In securing information for the report, Chamberlin picked up the December 31, 1959 balance sheet and profit and loss statement for Walker Motors-Kennewick and Walker Motors-Union Gap (Defendant's Exhibits A-32 and A-33) Chamberlin also secured from the Seattle-First National Bank, Richland Branch, a copy of

Palmer Walker's personal financial statement. A monthly operating statement was secured on Tri-City Rambler with the understanding that a more detailed statement was being prepared.

Chamberlin working with Denny Englund, an S. & R. employee, made a further determination that $11,770.00 in cars had been sold "out of trust". Flooring figures were secured both on the Walker Motors in Union Gap and Kennewick as well as Tri-City Rambler. (R. Vol. 9, p. 2041) The Strong report (Defendant's Exhibit A-19) gives quite an accurate picture as to the financial condition of the Walker corporations. It indicates total indebtedness to S. & R. of $232,998.00, of which $26,000.00 was delinquent; an additional flooring indebtedness to the National Bank of Commerce of $44,500.00; 1959 operating results of Walker corporations were shown as follows:

Walker Motor Company-Kennewick, loss	($6,000.00)
Walker Motor Company-Union Gap	4,072.00
Tri-City Rambler, loss	(7,900.00)
Combined loss	($9,828.00)

The delinquency of $25,925.00 is itemized emphasizing the $11,770.00 of cars sold "out of trust", a part of this delinquency; analysis is made as to what it would take to handle the Volkswagen flooring account in the way of financing. Page 3 of the report lists the alternative to taking on the full line, emphasizing that it would be

liquidation and further indicating that the loss on liquidation would be approximately $40,000.00. The report was very carefully read by Donald Sherwood as is indicated on the exhibit by Mr. Sherwood's initialing and checking as well as commenting on the report. The report was a combined effort of Robert Chamberlin and W. G. Strong with Chamberlin furnishing the information from the books and records in the S. & R. Kennewick office.

On cross examination Strong admitted that he did not suspect the figures and at no time stated that the figures were incorrect. (R. Vol. 8, p. 1756) In his conclusion, Strong recommended taking on the Volkswagen flooring for two reasons: (1) They would be able to pick up additional security in a net amount of approximately $50,000.00 and that this would be very helpful in the event of forced liquidation; and (2) that if the account was handled firmly it should be in such a position by the year end that they could dispose of it easily or they might retain the account and liquidate other less favorable business.

Although the report on its face indicated a very serious financial situation and one that was steadily deteriorating as far as the Walker enterprises were concerned, still no action was taken by Walla Walla either to authorize a new loan to the Walker corporations or to foreclose. Also about this time Donald Sherwood left for Europe, it being about the first part of April, 1960. (R. Vol. 8, pp. 1758-

1759) Chamberlin thought that it was necessary that the Walker dealership find a "home" for its flooring and business and that otherwise there would be a potential loss. He computed this loss to be in the neighborhood of $35,000.00 and wanted to chattel all of the holdings of the Walker corporations through a security arrangement so that S. & R. would be better protected. (R. Vol. 9, p. 2044)

Prior to Donald Sherwood leaving for Europe, Chamberlin appeared at an executive committee meeting in Walla Walla on February 29, 1960, and emphasized that action should be taken one way or the other upon the report; that either S. & R. should secure themselves or get out. Immediately after Chamberlin made this statement, Donald Sherwood took the meeting over and spent the rest of the time pointing out Chamberlin's errors during the last two or three years. (R. Vol. 9, pp. 2046-2047) Chamberlin did not have authority to enter into any dealer agreement with Walker but he had reached the determination that the account could be saved and there would be no loss as far as S. & R. were concerned. As indicated above, no action was ever taken by either Don Sherwood, Bert Edwards or Bill Strong as far as directing foreclosure on Walker or the making of the loan. (R. Vol. 9, p. 2048)

After Donald Sherwood left for Europe Chamberlin determined to go ahead as far as he was able in the loan

negotiations. He employed an attorney to work out a merger of Walker Motors-Kennewick and Tri-City Rambler, Inc., so that all personnel could be put in one shop and overhead could be cut down. Discussions were also had with Palmer Walker and with his attorney, Bob Day in this connection. (R. Vol. 9, pp. 2048-2050)

During the merger and loan negotiations with Walker and his attorney, Bob Day, Chamberlin was advised that Walker had checks out to Volkswagen of Washington, his prime supplier, and needed cash to cover them. Chamberlin then loaned Walker $9,000.00 on his personal note for two reasons: (1) he wanted to keep the dealership afloat, and (2) he didn't want any adverse publicity in the period of negotiations. Also, it was Chamberlin's thinking that in the event Walla Walla did not authorize the loan, that the $9,000.00 individual loan just made, plus the $15,000.00 personal guarantee on the loan of July 31, 1959, would enable S. & R. to attach all of Walker's stock in the Volkswagen corporations, together with all of his personal assets, if it was determined to liquidate the account. (R. Vol. 9, pp. 2050-2051) The $9,000.00 loan was made on May 2, 1960, and appeared on the finance loan register. (Page 5, Defendant's Exhibit A-10)

On May 9th or 10th, 1960, Chamberlin contacted Bert Edwards by phone advising him that they had a serious dealer situation he wished to discuss. Chamberlin then

went to Walla Walla on May 11th, taking with him Exhibit A-20, which was a new compilation of the Walker deficiencies prepared by Denny Englund for Bob Chamberlin on May 5, 1960. Exhibit A-20 sets forth a total deficiency for all three Walker corporations of $107,-258.49, with units sold "out of trust" in the amount of $46,888.78. This exhibit called attention to Walla Walla of how badly the Walker Motors corporations had deteriorated since the Strong report of February 15, 1960. Mr. Edwards sent W. G. Strong to Kennewick on May 12, and while Strong was in Chamberlin's office, Chamberlin received a phone call from Walker that he, Walker, had $35,000.00 "which he had secured from friends on the avenue and that if they had any intentions of criminal prosecution, they could forget them because he, Walker, was able to pay off the out of trust transactions." Edwards agreed to come up to Kennewick on the next day, Friday, May 13, 1960, and meet with Walker. (R. Vol. 9, pp. 2056-2058)

(9)

WALKER SECURES A $35,000.00 CASHIER'S CHECK FROM THE SEATTLE-FIRST NATIONAL BANK, RICHLAND, WITHOUT SECURITY

This bizarre transaction of Palmer Walker was made with Robert Hodgson, assistant manager at the Bank on May 12th, 1960. Walker who had done business with the bank for some years, advised Hodgson that he was

scheduled to have a meeting that same day with a Volkswagen distributor out of Seattle. That there was a possible business deal pending and that it might involve his needing some funds. That he was not sure, but that he was going to need $35,000.00 to take to the meeting with him, and if the deal went through he would have need of a $35,000.00 term loan. Walker further told Hodgson that if the deal didn't go through, he would return the $35,000.00 the same day. In other words, Walker wanted to borrow the money either for a day or for a term. Hodgson decided to let him have the money based upon his story and their previous experience with him and even though the Bank had had many overdrafts on Walker's account. (Defendant'sExhibit A-18) Late in the afternoon the $35,000.00 check was returned and the note previously signed by Walker was paid off from the proceeds of the cashier's check. (R. Vol. 7, pp. 1526-1527)

On May 13, 1960, Mr. Edwards came to Kennewick and a meeting was held with Edwards, Walker and Chamberlin present. The $35,000.00 cashier's check was exhibited by Walker to both Chamberlin and Edwards with Walker stating that, "Now, here I have money so let's get off the criminal prosecution thinking and get down to loan negotiations." Walker did not hand the cashier's draft to either Edwards or Chamberlin and nothing was said by Walker as far as applying it to any Walker corporation indebtedness. (R. Vol. 9, pp. 2058-2059)

After the meeting with Walker, Edwards and Chamberlin went to lunch and at that time Edwards brought up the $9,000.00 loan made by Chamberlin to Walker. Chamberlin was advised that in view of his exceeding the lending authority, his signature was being removed as an authorized signator at all of S. & R. banks in the Tri-City area. That further this was being done as disciplinary action. Chamberlin then told Edwards that under these circumstances he didn't feel that he could effectively act as manager of S. & R.'s Tri-City Branches and tendered his resignation, which was accepted. (R. Vol. 9, pp. 2059-2060)

One of the many inexplicable things about the $35,000.00 cashier's check episode, above set forth, is the fact that both Robert Hodgson and Joseph Stricker testified definitely that the entire transaction took place on May 12, 1960, while Bert Edwards and Robert D. Chamberlin were equally positive that the check was exhibited to them on Friday, May 13, 1960.

On May 23, 1960, Austin Roberts and Bert Edwards, members of the executive committee, held a meeting in Walla Walla. Chamberlin's resignation was discussed and reviewed as well as the circumstances of the Walker Motor Co. loan and commitment authority. It was noted upon this date that S. & R. had no disagreement with Chamberlin. (Defendant's Exhibit A-21, Minutes of Exe-

cutive Committee Meeting of May 23, 1960, Appendix, page 2)

(10)

LOAN NEGOTIATIONS OF BERT EDWARDS ON BEHALF OF S. & R. WITH PALMER WALKER

After Chamberlin terminated his employment with S. & R., Bert Edwards, on behalf of S. & R., continued negotiations with Palmer Walker in regard to a loan to the Walker corporations by S. & R. Edwards knew from the deficiency statement shown him by Bob Chamberlin on May 11th (Defendant's Exhibit A-20) that the Walker corporations were out of trust approximately $50,000.00. He further knew that the total deficiency was $107,000.00 plus the $9,000.00 unsecured loan of May 2, or a total of $116,000.00.

Discussions were had upon both May 24, 1960, and May 31, 1960. Edwards also knew that the financial statements of the Walker corporations had gone down as far as Walker's net worth was concerned $140,000.00. (R. Vol. 7, pp. 1641-1646) Mr. Edwards in his conversations with Walker and Mr. Walker's attorney, Bob Day, indicated that as soon as they received Walker's financial statements they could determine more the details and further stated that: "If we have to doctor them up that way, we are not reluctant to consider that, of course." (R. Vol. 7, p. 1647)

Edwards further agreed that the merger of the two corporations in Kennewick would be a good thing because it would cut down overhead and permit Walker to consolidate his accounting and further concentrate his operation on one premises. No definite agreement was reached in either of these meetings the latter part of May. (R. Vol. 7, p. 1648)

(11)

OWNERSHIP OF TRI-CITY RAMBLER STOCK BY ROBERT D. CHAMBERLIN

Appellant's argumentative statement of the case presents only S. & R.'s view of the Tri-City Rambler stock transaction. The facts in regard to the stock are as follows:

Chamberlin was initially contacted in January of 1959 by Walker in regard to Walker's estate plan, with Walker requesting that Chamberlin act as Trustee in his estate. At that initial conversation Chamberlin agreed to act as Trustee. Walker had been in S. & R.'s office on some routine business and brought the matter up. Next the estate matter was discussed at Walker's place of business, at which time Walker stated that his attorney had worked out a plan whereby the managers of Walker's three corporations were to run the business and that Chamberlin was to be the trustee and have authority over these men and was also to be issued stock in the corporation. (R. Vol. 9, pp. 2061-2062) On July 15, 1959, at

Walker's office, a third conversation took place and Walker advised Chamberlin that he had gone over the entire situation with his attorney and his attorney had advised him that naming of the other directors on the trusteeship by name was not a satisfactory situation and that they would be named by position, namely, the managers of his corporations, but that Chamberlin was still to have stock in the Rambler Company and be the governing member on the trusteeship. Walker further told Chamberlin at this time that in the event of his death, the corporations were to be operated until such time as they could be liquidated and his wife paid the proceeds.

Chamberlin was further of the opinion that his having a stock ownership would be beneficial to S. & R., because it would give S. & R. first-hand knowledge of the estate. At this meeting Chamberlin received ten shares of non-voting stock of Tri-City Rambler. At no other time did he receive stock in any of the other Walker corporations. Chamberlin was also instructed that he had no authority whatsoever in Walker's affairs until such time as the trusteeship came into being. (R. Vol. 9, pp. 2062-2065)

During the first part of June, 1960, it was reported to Chamberlin that Walker had told Donald Sherwood and other members of the executive committee, that Chamberlin had an interest in the Tri-City Rambler. Chamberlin requested a meeting for the purpose of clarifying his position. This meeting was held on June 7, 1960. At

this meeting Chamberlin told Donald Sherwood, Cameron Sherwood, Bert Edwards, Bob Day and Palmer Walker, who were in attendance, the facts as above set forth in regard to the Tri-City Rambler stock. The following day on June 8, 1960, he forwarded the stock in question by mail to Robert S. Day, attorney for Palmer Walker, the letter of transmittal being (Plaintiff's Exhibit 73—Appendix, page 1) The letter of transmittal clearly states and sets forth Chamberlin's position in regard to the stock, namely that he did not request the stock, pay for it or accept the stock in any way for financial gain. That further he did not want, nor would he accept any payment for the stock.

S. & R., through the members of its executive committee, continued negotiations with Palmer Walker with reference to working out a loan of some type, and although an oral agreement was thought reached on June 30, 1960, the negotiations finally blew up, due to various demands that were being made by S. & R. for the control of Walker's businesses. (R. Vol. 8, pp. 1861-1863)

(12)

S. & R.'S KNOWLEDGE AS TO FALSITY OF WALKER'S FINANCIAL STATEMENTS

St. Paul does not controvert the statement in S. & R.'s opening brief as to Edwards' first actual knowledge of the falsity of the Walker corporation's financial statements.

It is true that Mr. Edwards testified that technically his first knowledge of the falsity of the statements was obtained on May 27, 1960, when he examined C.P.A. Tame's work sheet financial statement. Long before this, however, S. & R. was familiar with the Walker Corporation's financial problems by reason of, first, the Strong report of February 15, 1960 (Defendant's Exhibit A-19) as well as Chamberlin's conference with Edwards on May 11, 1960, alluded to when Chamberlin brought to Edwards' attention the deficiency balance and increased "out of trust" situation as shown by Denny Englund's report of May 5, 1960 (Defendant's Exhibit A-20).

Although S. & R. in its opening brief argues on page 29 that Chamberlin by reason of being furnished copies of Walker corporations' financial statements and in turn furnishing those copies to the Seattle First National Bank, necessarily knew that the statements were false in view of his knowledge as to previous "out of trust" transactions; this argument and inference is not true as Chamberlin testified flatly that he had no knowledge as to any false entries in the Walker corporations books during Chamberlin's employment by S. & R. He also had no knowledge as to the falsity of the Walker corporations' financial statements until late April or early May, 1960, when it was apparent that the statements were not the same as the earlier Walker corporation financial statement. (R. Vol. 9, pp. 2070-2074)

(13)

THE WILLIAMS TRANSACTIONS

The various dealings that the S. & R. Tri-City offices had with Donald K. Williams are good examples of careless and inept operations on the part of S. & R. employees in both the Tri-City area and Walla Walla. S. & R. - Kennewick started dealing with Williams in the fall of 1956 when Chamberlin approved a small line of credit of five cars or $500.00 for Williams. Williams, at that time, was a small used car dealer. Through inadvertence or a "goof" this small line of credit was allowed to balloon up to the extent of $22,000.00 or $23,000.00. It was brought about by various men in the S. & R. - Kennewick office, all handling the Williams' account without apparently realizing the limitations that had been placed upon the account. (R. Vol. 2, pp. 387-389) The status of the account was brought to Chamberlin's attention by Dean Dion and Dion was instructed to immediately liquidate the account down. This was done and Dion got the account down to somewhere between $5,000.00 or $6,000.00, using rather drastic but firm methods. (R. Vol. 2, pp. 389-390) Unfortunately, while S. & R. - Kennewick was liquidating the Williams' account down, Williams unknown to S. & R. - Kennewick was making additional flooring loans at S. & R. - Pasco. Dave Clancy was manager of S. & R. - Pasco, but exercised very little supervision over the loans made to Williams. Clancey was transferred to Walla Walla in

the late spring of 1958 and Chamberlin became general manager of S. & R.'s Tri-City offices on July 22nd, 1958. (R. Vol. 1, pp. 54-56; R. 20 Pretrial Order) Apparently no liaison existed between Chamberlin in Kennewick and Clancey in Pasco. Chamberlin first became aware of the fact that Williams had been securing loans from S. & R. Pasco during the summer of 1958, after he became general manager. He then instituted the same practice in the Pasco Office that had been undertaken in the Kennewick office as far as liquidating Williams down to a reasonable amount. The loans to Williams in the S. & R. - Kennewick office were made during this period of time by Chamberlin, Marshal, O'Herin, Dion and Turnquist (Defendant's Exhibit A-26) In S. & R. - Pasco the loans to Williams were made by Koster, Mirus and Kruger (Defendant's Exhibit A-27) After investigation showed the true status of the Williams' account in both offices, S. & R. took various security from Williams, including a quit claim deed (Defendant's Exhibit A-3) an additional quit claim deed (Defendant's Exhibit A-5. The equity on the first deed was about $3,500.00 and the equity on the second deed was $5,000.00 or $5,500.00 (R. Vol. 2, pp. 399-400)

The consolidation of the Williams' loan took place in November 1958, when the security above mentioned was taken. The efforts to liquidate the account had not proven too satisfactory so that in June of 1959 Williams' business was sold by S. & R. to one John L. Hale who executed a

note in the amount of $5,000.00 which was then credited to the Williams' account. Hale operated a used car lot under the name of Quality Motors and was still operating it at the time Chamberlin left S. & R.'s employ. (R. Vol. 2, pp. 401-402)

During the period that Williams was securing flooring loans from both S. & R. in Pasco and Kennewick, and during the period of his liquidation, he was required to sell S. & R. repossessions generally without receiving a commission. He also worked on S. & R. repossessed cars that needed repair. This saved S. & R. money and was a good "deal" for S. & R. (R. Vol. 1, pp. 208-209) On cars sold by Williams for S. & R. employees, Williams not only received the repair costs, if repairs were involved, but also a commission for selling the cars. (R. Vol. 3, pp. 560-561)

Encouragement of employee loans was an important factor bringing about the employee car sales. Prior to 1958 there was no particular policy with reference to employees purchasing repossessed automobiles with the exception that the repossessed automobile was first offered to the company, and if the company did not purchase the car, the employee was free to go ahead and purchase it. In addition to Chamberlin, Dion and Koster buying repossessed automobiles, Dave Clancey the manager at S. & R. - Pasco, purchased repossessions. (R. Vol. 2, p. 378)

In November, 1958, at a branch manager's meeting in Walla Walla, Chamberlin brought up the matter of employee loans and moved that the loans be discontinued, or, as an alternative, that all employee loans be funnelled through Walla Walla. Chamberlin's motion at the meeting died, securing only one vote in addition to Chamberlins. Prior to the vote on the motion, Donald Sherwood spoke upon the matter of employee loans, stating that the total volume was in the neighborhood of $180,000.00 to $200,000.00 and that it was profitable loan business. That if the employees had this much business to generate, that the Company should be entitled to that business and deal with them. At that time the interest charged on employee loans was 8% but thereafter it was raised to 12%. (R. Vol. 2, pp. 381-382)

A bizarre feature of the Williams Transaction was the successive flooring in June and July, 1958, of two different Chevrolets. This involved John Koster, Jerry O'Herin and Mirus. Dean Dion also handled some of the transactions with Williams. The evidence does not indicate whether the loans were made on invoice or certificate of title. (R. Vol. 6, p. 1445) (R. Vol. 9, pp. 1972-1976) The motor numbers of the Chevrolets was not checked as they were brought in and re-floored, after having been paid off. (R. Vol. 9, p. 1973) It was out of this repeated flooring of the two Chevrolets that Williams passed several N.S.F. checks.

Although S. & R. called Williams as a witness, they did not inquire of him about the successive flooring transactions upon these two Chevrolets.

(14)

THE NICHOLSON CAR DEAL

The first car involved in this transaction was a 1957 Plymouth which was driven out from the factory for Chamberlin and then placed upon Williams' lot for sale. Williams sold the Plymouth to one Jessee who financed the car through S. & R. The proceeds of the loan Jessee made with S. & R. were applied to Chamberlin's account by which he originally financed the Plymouth. Jessee traded in a 1956 Austin on the Plymouth which at the time of the trade-in was incumbered at the National Bank of Commerce in Kennewick. This loan was paid off to the National Bank of Commerce by Chamberlin. Chamberlin drove the Austin as his personal car for some six or seven months. (R. Vol. 2, pp. 411-418)

Jerry F. O'Herin, employed by S. & R. - Kennewick from 1956 through the middle of 1959 as a small loan man, handled the transaction with Nicholson. Nicholson came into the Fairway Finance Office of Kennewick in November of 1957, having had a small loan balance with that office for some time. He had also another Fairway Finance loan at the Pendleton Office and wanted to consolidate the two loans, and obtain more money to purchase

an automobile. O'Herin suggested that Nicholson go to Pendleton and endeavor to make the loan there, as the Pendleton office had the largest balance. (R. Vol. 8, pp. 1792-1795)

Previous to this time, Chamberlin had been in correspondence with the Pendleton office of Fairway Finance attempting to work out a consolidation of Mr. Nicholson's loans between the two offices. Apparently this was unknown to O'Herin when he talked with Nicholson in November, 1957. Pendleton refused to consolidate the loans and O'Herin then went ahead with a consolidation of the loan in the Kennewick office. At this time Nicholson advised O'Herin that he wished to buy a car and O'Herin then asked Chamberlin if he was interested in selling his 1957 Simca. Chamberlin agreed to sell it and O'Herin proceeded with the handling of the transaction. A new consolidate loan was then made to Nicholson, paying off Pendleton, in the total amount of $3,923.28, as set forth on page 34 of appellant's brief. The purchase price of the Simca paid to Chamberlin was $1,740.62. It will also be noted that finance charges for this loan amounted to $771.16. As security for this loan, O'Herin chattel mortgaged the 1957 Simca, a 1951 Buick, an electric calculator, electric typewriter, television set, radio and a number of household items of furniture, together with a wage assignment. (R. Vol. 8, p. 1797)

On November 18, 1957, Nicholson paid $600.00 on the account. Shortly thereafter Nicholson returned the Simca to the office and an $1,800.00 credit was given him for the return of the automobile. (R. Vol. 8, pp. 1799-1800) There was a rebate to Nicholson of $454.21 of finance charges. This left $316.95 finance charges still a part of the loan. Although the rebate charges of $454.21 were credited to Nicholson's loan, the check was written directly to Fairway Finance-Kennewick, covering this item in accordance with the bookkeeping practices of S. & R. (Plaintiff's Exhibit 35) After the various credits of $600.00, $1,800.00 and $454.21 given Nicholson, this left a balance due on the original loan of $3,923.28, of $1,069.07. This was rewritten again in a new loan, the new loan being in the total amount of $1,831.92. The new loan was rewritten on February 27, 1958, or thereabouts. (Plaintiff's Exhibit 31) A breakdown of the new loan is shown on page 35 of appellant's brief, being the original balance of $1,069.07, additional cash by check to Gene Nicholson of $430.93, new finance charges of $244.91 and insurance item of $87.01.

Considering the previous finance charges of $316.95 which were still a part of this re-write, and the new finance charges of $244.91, S. & R. was to receive $561.86 finance charges on the loan of $1831.92. Chamberlin did not receive any moneys out of the Nicholson transaction with the exception of the original $1740.62 paid him out of the

first Nicholson loan. (R. Vol. 8, p. 1806) The 1957 Simca returned to S. & R. by Nicholson was then traded by Chamberlin to Walker Motors, together with Chamberlin's Austin for an MG. Chamberlin used this method of disposing of the Simca for S. & R. S. & R. was paid the value of the Simca that Chamberlin received on the trade-in of $1300.00 (R. Vol. 2, p. 426). Chamberlin paid the $1300.00 to S. & R. by making a loan with S. & R. on his MG.

Nicholson thereafter left the State of Washington and was adjudged a bankrupt in the State of Minnesota. (Plaintiff's Exhibit 28)

(15)

CHAMBERLIN'S CAR TRANSACTIONS

In 1958 Chamberlin received an inquiry from the Securities Acceptance Corporation regarding an automobile that this company had financed and which they wished repossessed. The automobile was picked up by Chamberlin and he secured bids from the various automobile dealers. The bids were forwarded to Securities Acceptance Corporation and they accepted the highest bid. Chamberlin then sent them a check of S. & R. which was charged to the Suspense Account and dated January 31, 1958. The car was placed on the Don Williams used car lot for sale. On March 6, 1958, a loan file was set up. Chamberlin did not pay S. & R. the 12% interest for the per-

iod of somewhat more than thirty days due to the fact that he was not in S. & R.'s office a great deal during this period of time. He was travelling a great deal, setting up trailer financing in Idaho and Eastern Washington. He testified he did not have any intent to defraud S. & R. of the 12% interest. (Vol. 2, p. 432) The Suspense Account check was in the amount of $1250.00.

The Mercury automobile was sold by Donald K. Williams on behalf of Chamberlin for $1525.87 plus a 1952 Hudson taken in as a trade-in. The sale of the Mercury by Williams was financed through S. & R. and apparently paid out without incident. The proceeds of the Mercury sale were credited to Chamberlin's loan account with S. & R.

The 1952 Hudson was sold to a Mr. Livingston for $325.00 by an S. & R. check being made payable to Mr. Livingston and then endorsed by him and redeposited in the S. & R. bank account. Some of the $325.00 apparently was paid to Mr. Williams and the balance to Chamberlin. (R. Vol. 2, p. 328) The car was repossessed from Livingston and then sold again to Clifton E. Blackburn. Blackburn was unhappy with the car and returned it and was repaid the purchase price. The $25.00 received by Chamberlin out of the re-sale of the Hudson was the difference between the Livingston purchase price and the Blackburn purchase price. (R. Vol. 2, p. 433)

As has been set forth, *supra,* employee loans were encouraged and there was no announced policy prohibiting employees from buying and selling repossessed automobiles. It was generally understood to be permissible. (R. Vol. 1, p. 58; pp. 187-189; pp. 206-207) The usual interest was charged employees on these transactions. (R. Vol. 1, p. 207) It was customary on all individual loans such as S. & R. financing an employee-owned car sold to a member of the public, for S. & R. to accept the paper without recourse to the employee former owner in the event the financing went bad in the same manner as a member of the public bringing in a car to be financed. (R. Vol. 8, pp. 1890-1892)

(16)

THE KILTHAU LOAN

This loan involves John Koster, while manager of S. & R.-Richland. Koster was asked by Federal Discount Corporation, an out of state finance company, to contact a borrower who was delinquent, the borrower being a soldier stationed at Camp Hanford, near Richland. Koster worked the account unsuccessfully and finally had to repossess the automobile, it being a 1956 Oldsmobile. Koster then got bids on the automobile from automobile dealers with the high bid being $925.00. Federal Discount accepted the high bid and Koster determined to purchase the car himself. These transactions took place in March

of 1958. Koster drove the automobile for a short while and was approached by Mr. Kilthau on purchasing the automobile. Kilthau was recommended to Koster by Dick Thrap, an office manager of a construction firm in the Tri-City area. Koster sought a credit report on Kilthau but could get no information on him. The car was sold for $1350.00 plus the finance charges, which brought the total contract up to $1640.00, the finance charges being at the simple interest rate of 12%. Of the $1350.00 purchase price, $925.00 of it was payable to the Federal Discount Corporation and the remaining $425.00 belonged to Koster, he having purchased the repossessed automobile. However, the check for $425.00 was made out to John Kilthau. Kilthau had previously signed all of the loan papers and when the checks were issued to complete the deal, Koster was unable to get hold of Kilthau and so signed John Kilthau's name. Koster admitted that this was wrong but stated, as was the fact, that the $425.00 involved actually belonged to him and not to Kilthau. If Kilthau had endorsed the check, he would immediately have had to negotiate it to Koster to pay for the automobile. (R. Vol. 1, pp. 43-50)

As stated, *supra*, the jury after hearing the conflicting evidence on the many transactions, found no dishonesty or fraud on the part of the four principals and so answered the interrogatories.

COUNTER-STATEMENT OF QUESTIONS INVOLVED

Appellant S. & R. in its specifications of error 1, 2 and 3, put in issue on this appeal the trial court's action in denying appellant's motion for a directed verdict and post trial motions. Questions thus raised should be restated in view of the fact that the case was submitted to a jury and a verdict favorable to the appellee rendered. The questions upon these specifications of error thus become:

(1) Was there any evidence or reasonable inferences from the evidence making the claim of fraud and dishonesty upon the part of the principals under the bond a question of fact for the jury?

(2) Is there any evidence or reasonable inference from that evidence substantiating the verdict of the jury finding the principals under the bond not guilty of fraud or dishonesty?

The remaining questions involving instructions to the jury and admissibility of evidence will be answered in the form set forth by the appellant S. & R.

SUMMARY OF ARGUMENT

1. The evidence clearly presented a question of fact for the jury and fully supported the verdict of the jury, finding the principals under the bond not guilty of fraud or dishonesty.

Interpretation of the bond, limits its coverage to fraud and dishonest acts and cannot be extended to include negligence, incompetence, carelessness, mismanagement or losses from bad debts.

2. The instructions of the court were correct and appellant's proposed instruction number 31 was properly refused.

Dishonest and fraudulent conduct cannot be extended to include a reckless, willful and wanton disregard for the interests of the employer.

3. The court properly exercised its discretion in refusing to strike the testimony of Robert Day relating to S. & R.'s loan negotiations with Walker.

The court was further correct in its discretionary ruling excluding the statement of Rivon Jones, representative of St. Paul, as to a certain admission attributed to Jones, which was in any event nothing more than Jones' opinion and was not a statement of fact.

ARGUMENT IN ANSWER TO APPELLANT

Before embarking upon an examination into the facts answering S. & R.'s argument that Chamberlin and Koster were dishonest as a matter of law, we should have in mind some of the fundamental principles involved in the review of a jury's verdict.

"The propriety of granting or denying a motion for a directed verdict is tested both in the trial court and on appeal by the same rule. The trial court must view the evidence and all inferences most favorable to the party against whom the motion is made. The reviewing court must do the same with respect to a judgment entered on a directed verdict or the denial of a motion for a directed verdict or a judgment entered notwithstanding the verdict. The decisions are many and the rule is the same both on appeal, and on the hearing of the motion in the trial court."

Vol. 2B, Barron & Holtzoff, Section 1075, page 378.

Schnee v. Southern Pac. Co., (C.A. 9, 1951) 186 F. 2d 745.

Graham v. Atchison Topeka & Sante Fe Ry. Co., (C.A. 9, 1949) 176 F. 2d 819.

In *Lavender v. Kurn (1946) 327 U. S., 645; 90 L. Ed. 916,* the United States Supreme Court stated in regard to the function of an appellate court in reviewing the verdict of the jury, that *(page 653 of U.S., and 923 of L. Ed.):*

"It is no answer to say that the jury's verdict involved speculation and conjecture. Whenever facts are in dispute or the evidence is such that fair-minded men may draw different inferences, a measure of speculation and conjecture is required on the part of those whose duty it is to settle the dispute by choosing what seems to them to be the most reasonable inference. Only when there is a complete absence of probative facts to support the conclusion reached does a reversible error appear. But where, as here, there is an evidentiary basis for the jury's verdict, the jury is free to

discard or disbelieve whatever facts are inconsistent with its conclusion. And the appellate court's function is exhausted when that evidentiary basis becomes apparent, it being immaterial that the court might draw a contrary inference or feel that another conclusion is more reasonable."

In reinstating the jury's verdict the Supreme Court further stated:

"The jury having made that inference, the respondents were not free to re-litigate the factual dispute in a reviewing court. Under these circumstances it would be an undue invasion of the jury's historic function for an appellate court to weigh the conflicting evidence, judge the credibility of witnesses and arrive at a conclusion opposite from the one reached by the jury."

The rule has long been in the State of Washington that in appeals from judgments entered upon verdicts of a jury the Supreme Court will review the evidence most favorable to the successful parties and all such material evidence must be accepted as true. That further the verdicts must stand unless as a matter of law, there is neither evidence nor reasonable inferences therefrom to sustain the verdicts.

Wines v. Engineers Limited Pipeline Co., 51 Wash. (2d) 487, 319 Pac. (2d) 563.

Gildesgard v. Pacific Warehouse Co., 55 Wash. (2d) 870; 350 Pac. (2d) 1016.

THE EVIDENCE AMPLY SUPPORTS THE FINDING OF THE JURY THAT CHAMBERLIN AND KOSTER WERE NEITHER DISHONEST NOR FRAUDULENT

While it is true that for the obligee to recover upon a fidelity bond such as is involved in the case at bar, there need not be such an act as would support a criminal conviction, nevertheless, there must be a showing made of a dishonest or fraudulent act. A surety indemnifying the obligee for the dishonest or fraudulent acts of the principals under the bond, is not, however, liable for negligence, incompetence, unwarranted extension of credit, losses from mismanagement, the use of poor business judgment or for mere debts arising out of such acts.

In *Parker Lumber and Box Company v. Aetna Casualty and Surety Company (1926) 140 Wash. 262; 248 Pac. 795*, the Washington Supreme Court stated at page 267 that:

> "It has also been held that such bonds are liable for loss resulting from fraudulent or dishonest acts of the employee, but are not liable for mere debts or losses resulting from mismanagement or the use of poor business judgment by the employee.
>
> *Monongahela Coal Co., vs. Fidelity & Deposit Co. of Maryland, 94 Fed. 732.*
>
> *Williams vs. United States Fidelity & Guaranty Co., 105 M.D. 490, 66 Atl. 495.*"

In defining the liability of a surety for the acts of

principals under the bond it is stated in *45 C.J.S.-Insurance, Section 802, page 853*, as follows:

> "Hence, except as to acts which are in violation of statute or express rule, or which in themselves constitute the misconduct insured against, liability is not imposed on insurer for the consequences of acts done in actual good faith, without intentional fault, including constructively or technically fraudulent acts innocently done, even though they constitute a breach of obligation by the person whose fidelity is insured to the beneficiary, nor is the insurer liable for a loss occasioned through mere negligence, or carelessness, nor is the insurer liable for a loss through inattention to business, mismanagement, mistake, bad judgment, incompetency, or other acts or omissions not fraudulent or dishonest."

World Exchange Bank vs. Commercial Casualty Ins. Co., 255 N. Y. 1, 173 N. E. 902, supports the view that the question of an employee's fraud or dishonesty is one properly submitted to a jury. Therein the trial court had ruled the employee's conduct "Dishonest" as a matter of law and thereafter had granted a new trial. The appellate court in affirming the order granting a new trial and holding that it was a jury question, stated, speaking through Justice Cardozo at page 903:

> "We think the quality of the act is not so obvious and determinate as to exclude opposing inferences. (Citing cases) Criminal the act was not, unless done with criminal intent (Citing cases). The presence of that intent is not, in the setting of these circumstances, an inference of law. The question is perhaps closer whether the act within the meaning of the policy must be said to be 'dishonest', for dishonesty within such

> a contract may be something short of criminality. (Citing cases). (Then follows the statement set forth on page 51 of appellant's brief) * * * * * If this standard is to govern, we think the quality of the teller's act is for the triers of the facts. *The act was a wrongful one, very likely a technical conversion, certainly a departure from instructions, but in the common speech of men there would be reluctance to describe it as flagitious or dishonest."* (Emphasis added)

With the above principles in mind, considering the fact that the evidence in the case at bar is highly conflicting throughout, the acts of the principals, Chamberlin and Koster viewed in the most favorable light under the evidence, clearly were neither dishonest nor fraudulent, and involved properly questions of fact for the jury.

On page 52 of appellant's brief it is charged that throughout the entire period of his employment Chamberlin consistently withheld material facts from his employer. This, of course, is not true. All of the loans that were made to the Walker corporations were routinely reported on the monthly finance loan register. (Defendant's Exhibit A-10) However, as we have previously pointed out, no one in executive authority in Sherwood & Roberts Inc. in Walla Walla bothered to look over the monthly finance loan registers to see what loans were being processed at the branches. (R. Vol. 5, p. 1224) In judging Chamberlin's acts the jury was certainly entitled to consider the fact that the Sherwood & Roberts Branch organizations were decentralized and managers such as Robert D. Chamberlin

were completely self-sufficient, with each manager in complete authority as to the area he served. (R. Vol. 5, pp. 1128-1129, testimony of Donald Sherwood) A manager having such complete authority is certainly not to be burdened with the obligation of reporting every problem to the executives in Walla Walla. The jury was fully justified in concluding that Chamberlin had the authority to proceed in the handling of the Walker corporation consolidated loans, using his best judgment.

Appellant asserts that Chamberlin should have advised as follows:

(1) That Walker was "out of trust" in 1958 and 1959.

It was neither necessary nor required as far as Chamberlin was concerned, to report the situation of Walker being "out of trust" in 1958 as this matter was taken care of by the loan consolidation of November 19, 1958 when both the European Motors and Walker Motors-Kennewick loans were collateralized by Chamberlin in using his best business judgment. (R. Vol. 9, pp. 2005-2007) The evidence is far from clear that the Walker corporations were "out of trust" in 1959 due to the mix-up at the American Motor Company's distributing office when cars were shipped without invoices and invoices were sent without cars. (R. Vol. 4, 877-878; R. Vol. 9, pp. 2033-2034)

(2) The full extent of Walker's "out of trust" sale of mortgaged cars in 1960 was revealed by Chamberlin to the

best of his knowledge. In assisting W. G. Strong prepare his report of February 15, 1960, Chamberlin gathered the information on units sold "out of trust", using the figures of Denny Englund as secured on all Walker Motors corporations. (R. Vol. 9, p. 2041) There is no proof whatsoever that Chamberlin knew more units had been sold without being paid for than was contained in the Strong report at the time it was made. Denny Englund further prepared the report for Chamberlin on May 5, 1960, (Defendant's Exhibit A-20) which Chamberlin used in his discussion with Bert Edwards in Walla Walla on May 11th, pointing out to Edwards the seriousness of the situation. (R. Vol. 9, pp. 2056-2058)

(3) The fact that Chamberlin made loans totalling more than $35,000.00 in November 1958, as pointed out *supra* was an exercise of Chamberlin's best business judgment in collateralizing the indebtedness of the Walker corporations arising out of the sale of units without paying for them. Chamberlin's actions were done entirely for the benefit and protection of S. & R., and were not done for the purpose of covering up anything. As a matter of fact, Bert Edwards in his loan merger and consolidation talks directly with Palmer Walker in the latter part of May, 1960, was attempting to do the same thing, only he was dealing with a much larger sum than $35,000.00.

(5) It is asserted that Chamberlin should have re-

ported the alleged "kiting" of checks between Chamberlin and Walker. The book overdraft situation was, of course, self-evident to Walla Walla at all times by reason of the daily cash reports, if Walla Walla had bothered to examine the daily cash reports. (R. Vol. 7, pp. 1651-1652) The shortage of funds was brought about by Walla Walla not forwarding sufficient moneys to Chamberlin to take care of the business already committed. The book overdraft situation was known to Walla Walla, however, and Donald Sherwood did not forbid Chamberlin to continue the practice but merely advised him that if he was caught in a bank overdraft, he would be "standing alone". (R. Vol. 9, pp. 2019-2020)

(6) Chamberlin's ownership of stock in the Tri-City Rambler has been fully explained in appellee's counterstatement of the case *supra* (page 27). The stock was accepted in good faith by Chamberlin so that he could assist, if necessary, in the management of Walker's estate. (R. Vol. 9, pp. 2061-2062)

(7 & 8) Complaint is further made on failure to notify Walla Walla of the reduction in the personal guaranty of Walker by $32,000.00 as a result of the loan consolidation of July 31, 1959, and the further release of Walker Motors - Kennewick of obligations by reason of this loan consolidation. Appellant completely overlooks the testimony with reference to the need for eliminating Walker Motors - Kennewick as a flooring account. The

matter was taken up with W. G. Strong by Chamberlin and it was agreed that Walker Motors - Kennewick would be so eliminated. To do this, it, of course, was necessary to release Walker Motors - Kennewick as far as its collateral security was concerned to enable Walker Motors-Kennewick to seek flooring elsewhere. This was self-evident. As has been emphasized before, the consolidated loan was reported on the monthly loan register (Defendant's Exhibit A-10) and further facts could have been had by Walla Walla for the asking.

It must be remembered further in considering the charge of the appellant as to lack of notice of certain transactions to Walla Walla, that a manual of procedure did not exist in the entire S. & R. organization, as Mr. Donald Sherwood did not believe in them. (R. Vol. 5, p. 1224) Consequently the managers had to proceed in all instances using their best business judgment and clearly no requirement ever existed to notify Walla Walla other than the usual business routine forms that were in all instances complied with.

(9) The $15,000.00 unsecured loan made in December, 1958, was made to Palmer Walker personally for a legitimate reason, namely, to acquire and purchase Rambler parts, equipment and accessories. (R. Vol. 5, pp. 1037-1038) This loan did appear on the loan register and within six weeks thereafter approximately $11,000.00 had been repaid upon the loan. The previous "out of trust"

transactions that were consolidated in November, 1958, had no relationship to this loan.

(10) The $9,000.00 personal unsecured loan made to Palmer Walker on May 2, 1960, was made by Chamberlin for the purpose of preventing the Walker corporations from having N.S.F. checks outstanding. The loan did appear upon the finance loan register and in any event was known to Bert Edwards shortly after it was made. The making of this loan at most indicated only a lack of good business judgment upon Chamberlin's part. No necessity existed to specially notify Walla Walla of the transaction.

(11) The Donald Williams consoldated loan on November 20, 1958, again represents a loan transaction that improved the position of S. & R. by taking of security from Williams for the delinquent flooring loans and N.S.F. checks. There again was nothing about this loan that required special notification to Walla Walla and it, as did all other loans, appeared on the monthly finance loan register.

(12) Complaint is made of Chamberlin borrowing money from S. & R. and engaging in buying and selling certain automobiles that were his personal cars. Employee personal loans were desired by S. & R. (R. Vol. 2, pp. 381-382) and it was customary for employees to buy repossessed automobiles, provided it was not determined

that S. & R. would keep the repossessed automobile for resale. (R. Vol. 2, p. 378) The failure of S. & R. by either directive or incorporating employee rules in a manual of procedure prohibiting both employee loans and the purchase and sale of repossessions, actually was the primary cause of the employee car transactions. S. & R. could have stopped it if they desired. There, of course, was an eagerness to benefit from the interest paid by the employees that motivated S. & R. to permit the employee loans.

(13) The use of S. & R. money by means of the Suspense account for a period of a month due to the Securities Acceptance Corporation transaction by Chamberlin, arose out of inadvertence by Chamberlin's travelling away from the office a great deal. This was a mere oversight that could occur in any office. (R. Vol. 2, p. 432)

(14) The Nicholson and Simca deal, as the counterstatement of the case set forth by the appellee indicates, has two entirely different and conflicting versions. Appellant refuses to accept any version but its own, which, of course, the jury chose not to believe. This was a disputed question of fact and under Jerry F. O'Herin's testimony (R. Vol. 8, p. 1806) Chamberlin received nothing except the original purchase price of the car of $1740.62. The claimed double payment sought to be established by the appellant was apparently given no weight by the jury.

(15) The use of the suspense account by employees was a bookkeeping procedure that was employed by the S. & R. office in Kennewick. It did not involve any dishonesty or fraudulent purpose as far as the employees were concerned but was merely a method of initiating a loan. No directives have been pointed out by S. & R. indicating that this was an improper procedure or likewise that it resulted in any loss to S. & R. If this procedure was not desired by Walla Walla, it should have been changed by either Mr. Strong or Mr. Priest during their routine audits of the Kennewick operations.

Citation is made by appellant of *Nailor vs. Western Mortgage Co., 54 Wash. (2d) 151; 338 Pac. (2d) 737,* upon the point that misrepresentation of the financial condition of third persons has been held to be fraud. In the Nailor case we have a direct misrepresentation by a mortgage company to a supplier that the mortgage company's contractor was of good financial stability. The case is obviously not in point with the situation in the case at bar. Chamberlin made no representations to S. & R., but as S. & R.'s manager exercised his own business judgment in making the loans in question. As a manager, these decisions were his to make and there was no requirement that he run to Walla Walla with every loan problem.

The case of *Hanson vs. American Bonding Co., 183 Wash. 390; 48 Pac. (2d) 653,* is also cited by appellant as being applicable. The principal under the bond in the

Hanson case was a bank employee that had been convicted of an intentional violation of the banking act by a jury. Upon his later trial to the court upon the bond, the trial court agreed with the jury that under the facts the employee had been dishonest. This case in no way changes the Washington rule that a bonding company is not liable for losses arising from mismanagement or the use of poor business judgment by the employee-principal.

Parker Lumber & Box Company vs. Aetna Casualty and Surety Co. (supra) p. 46.

Commencing on page 56 of appellant's brief, repetitious claims are again made of allegedly dishonest acts upon the part of Chamberlin. It is asserted that the alleged check "kiting" permitted Chamberlin to conceal his own overdrafts and critical financial plight of the Walker Companies in the month end reports to Walla Walla. This, it is submitted, is pure fiction as the daily cash report forwarded to Walla Walla and testified about in detail by Dennis C. Hayden, the accountant for all S. & R.'s Tri-City offices, (R. Vol. 7, pp. 1651-1652) clearly proves that Walla Walla, if they read the daily cash reports, was fully apprised of the situation at all times. Bert Edwards knew of the book overdraft situation in the Kennewick office, as did also Donald Sherwood. (R. Vol. 9, pp. 2019-2020) No deception whatsoever was involved in the exchange of checks with the Walker corporations.

Complaint is made by S. & R., in its brief, of Chamberlin's recommendation of Walker to the American Motor Company. No showing whatsoever has been made by S. & R. that the statement: "Mr. Walker's business practices have been beyond reproach", in any way caused S. & R. a financial loss. The statement was made by Chamberlin for the purpose of assisting Walker Motors to secure the Rambler Franchise, and was further made after consideration of the excellent consumer paper that S. & R. had received from the Walker corporation. (R. Vol. 4, p. 827)

Appellant claims that since Chamberlin knew that Walker sent a financial statement to American Motors in December of 1958, that he also must have known that the statement was false. Chamberlin testified that he had never seen the statement in question prior to the trial. (Plaintiff's Exhibit 68-A) (R. Vol. 9, p. 2014) The appellant's theory was, of course, argued to the jury but the jury refused to accept it.

Complaint is made as to Chamberlin's conference with Mr. Donald Sherwood in the latter part of January, 1959, regarding the drafting instructions with the American Motor Company. It will be remembered that the American Motor Company would not accept S. & R. as a finance Company but insisted that the sight drafts be presented either to a national finance company or a bank. The committment to Tri-City Rambler had already been

made by Chamberlin and the only thing that remained to be settled was the guaranty to the Seattle-First National Bank. When Chamberlin had the conference with Sherwood, he did not ask for authority on the flooring commitment. (R. Vol. 9, p. 2018) The Walker situation as far as the previous "out of trust" transactions were concerned, was a closed book, Chamberlin having collateralized the loan, and there was no requirement upon Chamberlin to go over past history with Donald Sherwood. What Sherwood would have done if he had all of the facts, of course, is speculation. The testimony is in direct conflict as to what was discussed at the conference between Chamberlin and Sherwood in Walla Walla and the jury determined not to follow S. & R.'s theory of the evidence.

The July 31, 1959, loan consolidation, as has been emphasized *supra,* was made for the primary purpose of accommodating the tight money situation as far as S. & R.-Kennewick was concerned. The making of the loan and the release of Walker Motors-Kennewick as a dealer requiring heavy flooring commitments, permitted S. & R. in Kennewick to return to Walla Walla approximately $125,000.00 within the next 90 days. (R. Vol. 9, p. 2033; R. Vol. 7, p. 1653) There was no proof whatsoever that this transaction was intended as a further "cover-up" of the prior consolidation in November, 1958. It is asserted that Walker's personal guaranty was virtually eliminated. This,

of course, is not true as the loan of $47,716.90 was personally guaranteed by Palmer Walker in the sum of $15,000.00. (R. Vol. 9, pp. 2027-2028) Chamberlin in making this loan further determined that the total valuation of all the security was $61,313.25. (Plaintiff's Exhibit 58) There is no doubt that this loan was adequately secured. What brought about the very substantial loss was the refusal of Walla Walla to take action when action was required. The Strong report of February 15, 1960, emphasized clearly the desperate need for immediate action in regard to either closing out or refinancing the Walker corporations. Donald Sherwood left for Europe in April of 1960, and the subordinates under him let the situation steadily deteriorate until the deficiency reached over $107,000.00 as shown by Exhibit A-20. The vacillation of Walla Walla greatly increased the extent of the loss.

The argument is made that collusive misrepresentations arose out of the Chamberlin-Walker transactions. It is difficult to understand how such a contention can be made in view of the fact that all loans appeared on the loan register (Defendant's Exhibit A-10); that further W. G. Strong was notified as early as the spring of 1959 of the fact that Walker Motors had been selling cars in the previous year without paying for them and the further fact that Strong was furnished the information by Chamberlin of "out of trust" transactions for Strong's report of February 15, 1960. These acts are certainly not those of

a person seeking to conceal the situation from his superiors. Chamberlin's stock transaction has been fully explained and the jury obviously accepted Chamberlin's testimony in regard to it.

Chamberlin, in his capacity as manager for S. & R.'s corporations in the Tri-City Area, was in a fiduciary capacity and perhaps S. & R. had a civil action for negligence or perhaps mismanagement against Chamberlin. However, they do not have a cause of action for fraud or dishonesty that can be maintained. This entire case factually is based on conflicting evidence presenting a series of questions of fact for the jury's determination. The jury has made such a determination and its finding is conclusive and binding upon the appellants herein, with the evidence fully supporting the jury's verdict.

INTERPRETATION OF THE BOND

Appellant points out that a bond, such as before the court in the instant case, is to be broadly construed and protects an employer against the wrongful acts of an employee, even though not criminal. Appellee generally has no quarrel with the theory of broad construction on coverage or, as it is often stated in the converse, strict construction against the bonding company, but nevertheless wishes to emphasize that broad construction does not mean a re-writing of the bond.

St. Paul protected S. & R. under the bond against

dishonest or fraudulent acts of the principals. The bond is not an errors and omissions policy covering negligent or careless acts of the principals as appellant seems to contend. It is a fidelity bond protecting the obligee from loss by the intentionally dishonest or fraudulent acts of the principals.

In *Brown vs. Underwriters at Lloyd's, 53 Wash. (2d) 142; 332 Pac. (2d) 228,* the Washington Supreme Court stated as follows:

> "Over a hundred years ago, the supreme court of North Carolina in Tilghman v. West, 43 N.C. 183, 184, declared:
>
> '". . . Fraud cannot exist, as a matter of fact, where the intent to deceive does not exist: for it is emphatically the action of the mind which gives it existence . . .'"
>
> "Black's Law Dictionary (4th Ed.) 788, 789, says of fraud:
>
> '"It (fraud) consists of some deceitful practice or willful device, resorted to with intent to deprive another of his right, or in some manner to do him an injury. As distinguished from negligence, it is always positive, intentional . . .'"

In the *Brown* case, supra, the court was considering an errors and omissions policy that excluded dishonesty and fraudulent acts. In further considering whether or not the acts in question were excluded under the policy the court stated:

"It cannot be over emphasized that we are here dealing with an exclusionary clause which excepts from coverage losses 'brought about or contributed to by the dishonest, fraudulent, criminal or malicious act or omission of the assured or any employee of the assured . . .'

"Fraud in this connection must embrace dishonesty."

In *Dunlap v. Seattle National Bank, 93 Wash. 568; 161 Pac. 364,* the Washington court said:

". . . If when all of the facts and circumstances are taken together they are consistent with an honest intent, proof of fraud is wanting."

In *Irvin Jacobs & Co. vs. F. & Deposit Co. of Md., (C.A. 7) 202 Fed. (2d) 794; 37 A.L.R. (2d) 889 (1953),* quoted with approval in the *Brown* case, supra, the court of appeals for the 7th circuit stated:

". . . However, mere negligence, mistake or error in judgment would not ordinarily be considered a dishonest act. Acts resulting from incompetence cannot be characterized as dishonest."

In the cases cited by appellant, particularly *Mortgage Corporation of N. J. vs. Aetna Casualty & Surety Company, 115 A. (2d) 43; United States Fidelity & Guaranty Company vs. Egg Shippers S. & F. Co. (C.A. 8) 148 F. 353;* and *Md. Casualty Co. vs. American Trust Co. (C.A. 5) 71 F. (2d) 137,* there is no support for the contention that the dishonest or fraudulent act must not necessarily be an intentional act.

In the New Jersey case the court was dealing with admitted derelictions intentionally done and so stated in the following language:

> "It seems to us that in the instant matter we likewise could not properly stand by and permit the jury finding that the *admitted* derelictions of Harrison were not dishonest within the bond coverage. *We are not dealing with an instance of neglect, mistake or incompetence; nor are we dealing with an isolated inadvertent or insignificant delinquency by an employee. What Harrison did was done wilfully and was done over a period of four months.*" (Emphasis added)

In the *United States Fidelity & Guaranty Company* case the employee, as is pointed out in the citation quoted by the appellant on page 63: "was wilfully, intentionally and grossly faithless'.

In the *Maryland Casualty Company* decision the Bonding Company did not make any claim that the loss was brought about by the employee's negligence, error in business judgment or carelessness. A conspiracy was therein involved whereby the Bank president conspired with others "admittedly known to him to be insolvent" and made loans to such insolvent persons with the intention that they buy stocks which would then be jointly owned with the Bank president.

Proof of intent on the part of the principals, under the bond, to defraud S. & R. or to be dishonest in their employment by S. & R. was clearly lacking under the facts

and the jury was fully justified under the evidence in answering the interrogatories the way they did. The court likewise in view of the evidence properly submitted the case to the jury and there existed no basis either under the law or the facts to reverse the verdict of the jury.

THE NICHOLSON CAR TRANSACTION

This transaction has already been discussed twice by appellee in its brief and we do not intend to belabor the issue. As previously pointed out, the jury fully considered this transaction under the evidence and determined it adversely to the appellant. The evidence was conflicting and the jury chose to follow Jerry F. O'Herin's testimony rather than accept as the facts the bookkeeping advanced on behalf of the appellant. It must also be remembered that this rather complicated transaction took place 4½ years before the trial and it is understandable the difficulty witnesses had in remembering all of the precise details.

Appellee does wish to point out that O'Herin acting on his own gave Nicholson an $1,800.00 credit when Nicholson returned the Simca. It later developed that Chamberlin in his effort to realize on the car for S. & R. was only able to secure $1,300.00 and this by way of the trade-in method. The error in giving Nicholson too great a credit was not Chamberlin's but was O'Herin's. The fact that the Nicholson car transaction turned out to be a loss

for S. & R. cannot be used as a basis, as appellant is seeking to do, for the charge of dishonesty and fraud leveled against Chamberlin. The type of customers that S. & R. necessarily dealt with, due to the extremely high rates of interest, (as compared to commercial bank rates) necessarily invited risks of poor loans. (R. Vol. 2, pp. 439-442) The stable individual borrower or automobile dealer with good financial backing would obviously not deal with S. & R. and pay 12% interest when he or it could secure financing at a much lower rate from commercial banks.

Appellant continuously makes the charge of dishonesty and fraud but points to no undisputed evidence supporting such charges. It had its day in court and the jury simply did not believe or accept appellant's theory of the case.

Koster's endorsing of the check to Kilthau, while technically wrong, was not fraudulent or dishonest. It caused S. & R. no loss whatsoever; as we have previously pointed out, the money involved in the check actually belonging to Koster in any event.

The trial court's refusal to grant appellant's motion for a directed verdict and post trial motions was correct.

THE INSTRUCTIONS AS GIVEN WERE CORRECT AND THE TRIAL COURT PROPERLY REFUSED PLAINTIFF'S REQUESTED INSTRUCTION No. 31

To assist the court in considering appellant's speci-

fications of error 4 and 5 which relate to instructions given and proposed, appellee has set forth in its appendix all of the instructions of the court with the exception of stock instructions, that are not involved in this appeal. (App. pp. 4 to 10)

Appellant complains of certain portions of the instructions relating principally to the definition of dishonesty and also the requirements upon the appellant as far as proving either fraud or dishonesty. The questioned instructions are printed in italics in the appendix herein. (App. pp. 4 to 6)

Complaint is made that although the bond uses the words "fraud or dishonesty" in the disjunctive, the court did not submit these two terms in the alternative. This, of course, is not true, as a reading of the instruction will readily reveal. The cases do hold, however, that fraud does embrace dishonesty and that is the law in the State of Washington. *Brown v. Underwriters at Lloyd's, 53 Wash. (2d) 142, 322 Pac. (2d) 228.*

Complaint is also made because the court required proof of intent to defraud or intent to be dishonest. Intent is an integral part of either fraud or dishonesty and one cannot be unintentionally fraudulent or dishonest.

No cases have been cited supporting appellant's position that intent is not required in the proof of either fraud

or dishonesty. The Washington rule clearly requires intent. *Brown vs. Underwriter's at Lloyd's*, supra, page 61

It is stated in *45 C.J.S., Insurance, Section 802, page 852* that:

> "The terms 'fraud' and 'dishonesty' include any acts which show a want of integrity or a breach of trust. However, where the offenses named are one which commonly denote consciously wrongful conduct or involve moral turpitude, protection is intended against some positive act of wrongdoing, some form of dishonesty and the conduct causing the loss must involve some such characteristics to be within the bond."

In *Foster vs. Bowen, 311 Mass. 359; 41 N.E. (2d) 181*, the court in commenting upon the coverage of fidelity bonds and the construction of them stated:

> "The coverage of the bonds is not limited to strictly criminal acts. But the bonds were intended as protection against dishonesty and not as security in the ordinary sense for a balance which an accounting might show to be due. There is significance in the collective use of the expressions selected to define the coverage. All of them commonly denote conduct that is consciously wrongful. Indeed, only the words 'fraud', 'fraudulent', and 'misappropriation' seem capable of any other meaning, and these words must be defined with reference to the context in which they appear. *There is to be discerned in the decided cases a tendency to construe bonds worded as these are as insuring against the consequences of conduct of the employee that is intentionally and consciously dishonest and fraudulent and as not insuring against the consequences of acts done in actual good faith without intentional fault.*" (Citing cases)

* * * * *

> "In our opinion the bonds did not cover acts as were in fact innocently done and were merely constructively or technically a 'fraud', or 'fraudulent', even though they might constitute a breach of Cushing's obligations as an officer of the company and so give rise to a cause of action against him."

It is asserted that the appellant's proposed Instruction No. 31 correctly sets forth the law that reckless, wilful and wanton disregard for the interests of an employer palpably subjecting him to likelihood of loss is in law dishonest. An examination of the cases cited by appellant in support of this contention on page 59 of its brief reveals that the cases do not state that reckless or wanton conduct is sufficient proof of dishonesty but in practically every instance reiterate the rule above stated that intentional misconduct and intent are a requirement.

On the other hand, the following cases and states support the majority rule that the surety or indemnitor is liable only for intentional acts of dishonesty and intentional fraud as distinguished from mere wanton and reckless disregard for the employer's interests.

Also from *Massachusetts,* there is the case of *Gilmour v. Standard Surety and Casualty Company of New York, 292 Mass. 205; 197 N. E. 673.*

2. *Alabama:*

Louis Pizitz Dry Goods v. Fidelity & Deposit Co., of Maryland, 223 Ala. 385; 136 So. 800.

3. *Arkansas:*

United States Fidelity & Guaranty Co. v. Bank of Batesville, 87 Ark. 348; 112 S. W. 957.

4. *California:*

Taylor v. DeCamp, 132 Cal. App. 640; 23 Pac. (2d) 61 (Cites 25 C. J. 1093)

5. *Colorado:*

American Surety Company of New York vs. Capitol Building & Loan Association, 97 Colo. 510; 50 Pac. (2d) 792.

6. *Georgia:*

Massachusetts Bonding and Insurance Company v. Raskin, 43 Ga. App. 582; 159 S. E. 778.

7. *Indiana:*

Sparta State Bank v. Myers, 117 N. E. 258.

(" Such bonds insure the employee fidelity not his skill.")

8. *Iowa:*

(1) *Andrew v. Hartford Accident & Indemnity Company, 207 Iowa 652; 223 N. W. 529.*

(2) *Birrell Inc. v. Fidelity & Casualty Company of New York, 188 N. W. 26.*

9. *Kansas:*

(1) *Aetna Building and Loan Association v. Central Surety and Insurance Corporation of Kansas City, Mo., 145 Kans. 622; 66 Pac. (2d) 577.*

(2) *Kansas Flour Mills Co. v. American Surety Co., 98 Kan. 618; 158 Pac. 1118.*

10. *Kentucky:*

Home Owned Stores v. Standard Accident Insurance Company, 256 Ky. 482; 76 S. W. (2d) 273.

11. *Louisiana:*

(1) *Crescent Cigar and Tobacco Co. v. National Casualty Company, 155 So. 505.*

(2) *Curran and Treadaway v. American Bonding Company of Baltimore, 193 La. 763; 192 So. 335.*

12. *Minnesota:*

Village of Plummer v. Anchor Casualty Company, 240 Minn. 355; 61 N. W. (2d) 225.

13. *Missouri:*

Bank of Hammond v. Garner, 235 S.W. 822.

14. *Mississippi:*

Seelbinder v. American Surety Co., 155 Miss. 21; 119 So. 357.

15. *New Jersey:*

Mortgage Corporation of New Jersey v. Aetna Casualty and Surety Company (Cited and discussed above)

16. *New York:*

(1) *Bank of Edgewater N. J. v. National Surety Company, 243 N. Y. 34; 152 N. E. 456.*

(2) *World Exchange Bank v. Commercial Cas. Co., 255 N. Y. 1, 173 N. E. 902.*

17. *Pennsylvania:*

(1) *Universal Credit Company v. United States Guaranty Company, 321 Pa. 209; 183 Atlantic 806.*

(2) *Bank of Erie Trust Company v. Employers Liability Ins. Corp., 322 Pa. 132; 185 Atlantic 224.*

18. *Rhode Island:*

Jamestown Bridge Comm. vs. American Empire Insurance Co. 85 R. I. 146; 128 Atlantic (2d) 550.

19. *South Carolina:*

Salley vs. Globe Indemnity Company, 133 South Carolina 342; 131 S. E. 616 (43 A.L.R. 971)

20. *Tennessee:*

Fidelity-Phenix Fire Insurance Company of New York v. Jackson, 181 S. W. (2d) 625.

21. *Texas:*

American Surety Co. v. Gracey, 252 S. W. 263.

22. *U. S.:*

(1) *Irvin Jacobs & Company v. Fidelity & Deposit Company of Maryland (C.A. 7) 202 Fed. (2d) 794.*

(2) *Sade vs. National Surety Corp. (D. C. of D. C. 1962) 203 F. S. 680.*

23. *Wisconsin:*

Humbird Cheese Co. v. Fristad, 208 Wisc. 283; 242 N. W. 158.

("Wilful" as used, implies "purpose to do act and do wrong and implies an evil intent".)

Thus, if we go back to the Parker case in Washington we find 24 jurisdictions definitely favor appellee's position herein.

The court in its instructions defined in considerable detail the relationship of employer and employee and pointed out the duties upon the part of the employee to the employer. The jury was instructed to consider the breach or breaches, if any, of the duties set forth in making their determination as to whether or not the principals were guilty of fraud or dishonesty. (Appendix, pp. 6 to 8) It is thus apparent that the appellant's theories of the case were submitted to the jury albeit not in the precise language sought.

The instructions also referred to omissions of the principals and therefore the point of passive dishonesty

was obviously covered. Referring again to the interrogatories (R. pp. 129-132) fraud and dishonesty were submitted to the jury in the alternative, and if the jury found that the principals were guilty of either fraud or dishonesty, they were instructed to answer the interrogatories in the affirmative. The fact that the interrogatories were not separately put to the jury is of no consequence.

There was no error in the instructions.

THE COURT CORRECTLY RULED ON REFUSING TO ADMIT CERTAIN EVIDENCE AND LIKEWISE REFUSING TO STRIKE OTHER TESTIMONY

The errors asserted upon the evidentiary rulings are set forth in specifications of error 6 and 7. It is claimed that certain statements attributed to Rivon Jones, Claims Superintendent of St. Paul, who was present throughout the trial, should have been admitted. These statements were sought to be introduced in evidence through Donald Sherwood, although, as stated above, Mr. Jones was present throughout the trial.

It is claimed that Jones stated to Sherwood in effect that Chamberlin and Walker were in it together and both should have joint rooms at the state penitentiary. That further, S. & R.'s reputation was such that it couldn't be associated with two crooks like Walker and Chamberlin. It is obvious that these claimed admissions are nothing more than statements of opinion and not of fact. They

are not a part of the res gestae as no attempt was made to connect them up time-wise with the transactions.

In *Liljeblom vs. Department of Labor & Industries, 57 Wash. (2d) 136; 356 Pac. (2d) 307*, it was held that it was reversible error to admit the statements of a doctor employed by the defendant Department of Labor and Industries, such statements having to do with the doctor's dignosis that the claimant needed further treatment, was totally disabled, etc., the court holding that the statements were not binding upon the Department because they were the witness's opinions only. On page 143 the court stated:

> "An agent's statement to be admissible in evidence against his principal, must be a statement of fact and not the expression of an opinion. Albertson v. Chicago, Milwaukee, St. Paul & Pac. R. Co., 242 Minn. 50, 64 N.W. (2d) 175, 42 A.L.R. (2d) 1044 (1954); Borden v. General Ins. Co., 157 Neb. 98, 59 N.W. (2d) 141 (1953); Romo v. San Antonio Transit Co., (Tex. Civ. App.) 236 S.W. (2d) 205 (1951); Briggs v. John Yeon Co., 168 Ore. 239, 122 P. (2d) 444 (1942); Edwards v. Maryland Motor Car. Ins. Co., 204 App. Div. 174, 197 N.Y.S. 460 (1922); 31 C. J. S. 1113, § 343. The only portion of the report to which appellant objected contained Dr. Steele's opinion. The opinion evidence was not admissible."

In re *Allen's Estate, 54 Wash. (2d) 616; 343 Pac. (2d) 867*, the court quoted from the concluding paragraph of *31 C.J.S. 958, Section 217*, as follows"

> " . . . (1) Declarant must be unavailable as a witness. (2) The declaration must have related a fact against the apparent pecuniary or proprietary interest of de-

clarant when his statement was made. (3) The declaration must have concerned a fact personally connizable by declarant. (4) The circumstances must render it improbable that a motive to falsify existed . . . "

It is thus apparent that the testimony of the alleged admission by Mr. Jones was properly excluded because Mr. Jones was not only present in court but the statement at most was merely his opinion and would have been a flagrant invasion of the province of the jury.

Appellant does not argue its specification of error number 7, but in answer to this specification of error appellee wishes to point out that it involved a discretionary matter for the court to determine.

The testimony of Robert Day was material and proper and concerned negotiations between S. & R. and Palmer Walker. It involved testimony of S. & R. attempting to accomplish a consolidation of the Walker corporation indebtedness arising out of deficiencies. It was proof of S. & R. attempting to accomplish the same thing that they have criticized Chamberlin so bitterly for, namely, Chamberlin's consolidation of the Walker deficiencies in November, 1958, and his consolidated loans with Walker Motors at Kennewick on July 31, 1959. On both evidentiary rulings the trial court was correct.

CONCLUSION

Appellee respectfully urges that the entire case in-

volved conflicting evidence and conflicting theories that were fully and fairly tried and presented to the court and jury. That the applicable law was correctly stated in the instruction to the jury and that the jury thereupon rendered its verdict by answering interrogatories favorable to the appellee. Substantial evidence exists in support of the jury's verdict and this court, even in the event it should have different views of the evidence than the jury, nevertheless must accept the jury's verdict as being final and conclusive. The verdict of the jury and rulings of the trial court should in all respects be affirmed.

Respectfully submitted,

FRED C. PALMER
Of Palmer, Willis & McArdle
Attorneys for Appellee

April 20, 1963

I certify that in connection with the preparation of this brief I have examined Rules 18 and 19 of the United States Court of Appeals for the Ninth Circuit and that, in my opinion, the foregoing brief is in full compliance with those rules.

FRED C. PALMER
Attorney for Appellee

APPENDIX

OF

APPELLEES

Pls. Ex 73

Kennewick, Washington
June 8, 1960

Mr. Robert S. Day
Attorney at Law
1329 Geo. Wash. Way
Richland, Washington

Re: Stock — Tri City Rambler Inc.

Dear Bob:

I am enclosing the stock certificate issued to me covering Ten (10 Shares of Capital Stock in Tri-City Rambler Inc. You will find it properly endorsed for disposition.

I did not request this stock, I did not pay for this stock, I do not want this stock, I objected to the issuance of this stock.

I assume this stock can be taken off the books in the same manner that it was put on the books.

I did not consent to hold this stock for any financial gain, and further explained that I could not accept any financial gain. I will not accept any payment for this stock.

I trust your disposition of this stock will end what has been an embarrassing and disgusting delay in the negotiations of your client.

Very Truly Yours,

R. D. Chamberlin

bcc/Donald Sherwood

Defs. Ex. A-21

SHERWOOD & ROBERTS, INC.

Post Office Box 1020 106 North Second Avenue Telephone JA 5-3500
WALLA WALLA, WASHINGTON

To Executive Committee Date 5-23-60

From Bert R. Edwards

Subject Executive Committee Meeting
May 23, 1960

Meeting convened at 12:00 noon with Roberts and Edwards present.

The following matters were decided and agreed upon:

1. The salary adjustment for Theodore M. Schmidt from $400 to $450 per month, effective June 1, was approved. This action takes the place of the adjustment made May 9.

The following subjects were discussed and reviewed:

1. *Tri-City offices.* Robert Chamberlin's resignation as of May 13 was duly noted and the circumstances of the Walker Motor Co. loan and commitment authority were discussed. Edwards reported his conversations with Robert Chamberlin on May 19 concerning Cabadab, termination pay, radio station KYSS, the license application at Richland, the Mad Turk suit, etc. *We have no disagreement with Chamberlin.* (Emphasis added)

   It was noted that Chamberlin gave John Thompson a cash credit for 1959 vacation which Thompson had not taken, running said credit through the real estate register for March.

   Dave Clancy is continuing to assist John Koster in

the management of the Tri-City offices. Chamberlin has moved out.

W. G. Strong is applying himself to a clean-up campaign at Kennewick.

The lease on the Pendleton office was approved subject to criticisms listed in a formal letter to that office.

2. *Dean Dion.* Our relationship with Dion has been terminated. Dave Clancy having supervised the conclusion of the matter by taking title to two lots in Pasco for Dion's indebtedness in the approximate amount of $3,400.00 and by giving Dion a check for $255.00 for his ownership of 25% of the capital stock of Cabadab. It is noted the lots were appraised by James Aylward and Ken Brown at $3,500.00.

3. *Bonus Recommendations.* It was noted that bonus recommendations have been received from all of our offices since the last meeting of the Executive Committee.

4. *Position of Manager at Tri-City Area.* Applications have been received from James Aylward, Charles Erwin, John Koster, and Warren Hartley, each having been acknowledged to the applicant.

5. *Yakima office.* The request of the Yakima office for an increase in finance loan volume was discussed.

Meeting adjourned at 1:30 p.m.

nl
cc Gordon Johnson

(R. Vol. 10, pp. 2299-2306)

COURT'S INSTRUCTIONS IN PART

The terms "Fraud" or "dishonesty", as used in the bond, are to be given their usual meaning as the ordinary person understands them. However, I will give you a brief definition of each which should aid in guiding your understanding of these words as they are used in the bond.

Fraud consists of some deceitful practice or willful device, resorted to with intent to deprive another of his right, or in some manner to do him injury. As distinguished from negligence or an injury caused by thoughtlessness, it is always intentional. Fraud in its very essence requires a preconceived intention to deprive another of some property or money.

Dishonesty likewise consists of some intentional act which is committed with the foreknowledge that injury will result or is likely to result to another person. A dishonest act may be done with the hope that it will go undetected or that no harm will result but it is nonetheless dishonest. Dishonesty is included in fraud. An integral part of each act is an intent to deceive.

The term "connivance" likewise should be given the usual meaning as the ordinary person understands it to be. This definition, though, may be helpful to you: "Connivance relates to an agreement or consent, indirectly given, that something wrongful shall be done by another." In

other words, it defines a situation where one person knowing another is doing wrong, allows such conduct to continue without interference.

As you will recall, the parties have agreed that only fraud and dishonesty need be considered in this case. This is because the other bond provisions, to-wit, forgery, theft, larceny, misappropriation and wrongful abstraction, all are equivalent to dishonesty and fraud as I have defined those words. Thus, it is not necessary for the plaintiff to establish that any of the four principals was guilty of a criminal act, or that he would be subject to criminal prosecution of any kind. Therefore, if you find that fraud or dishonesty, or both, including intent to defraud the plaintiff, have been proved to your satisfaction by a fair preponderance of the evidence as to any of the plaintiff's contentions which I recited earlier, the plaintiff has sustained its burden of proof as to such contention or contentions. However, if you find that neither fraud nor dishonesty, including intent to defraud the plaintiff, have been proved to your satisfaction by a fair preponderance of the evidence, then in that event the plaintiff has not sustained its burden of proof as to such contention or contentions.

Fraud in its nature is not a thing readily susceptible of direct proof. Fraud must, in its very nature, usually be proved by inferences and circumstances shown to have been involved in the transactions which are in question. The same is true with respect to dishonesty. In this regard

I instruct you that it is reasonable to infer that a person ordinarily intends all the natural and probable consequences of acts knowingly done or knowingly omitted.

In your consideration of this case you must presume that all men are honest and that individuals deal fairly, that private transactions are fair and regular, and that participants act in honesty and good faith. This presumption must contoinue to guide you until you are satisfied to the contrary.

There is no liability under the bond and the law does not impose any liability on the part of the defendant for neglect, incompetence, the unwarranted extension of credit, losses resulting from mismanagement or the use of poor business judgment by any of the principals covered under the bond. Also, there is no liability for mere debts arising out of the acts or omissions of any of the principals.

In short, if you find that the acts or omissions which the plaintiff claims were dishonest and fraudulent were instead only the unfortunate result of good faith transactions, then the plaintiff has not sustained its burden of proof.

As to each of the contentions involving alleged dishonesty or fraud, you will consider all of the facts and circumstances in the evidence, including the relationships of the said principals to their employer and to each other, and to third persons or parties who were referred to or connect-

ed with any transaction or occurrence revealed by the proof.

The relationship of employer and employee requires the following duties upon the part of the employee to the employer:

1. That an employee is not to seek personal gain, with with respect to his employment, beyond his agreed compensation without first disclosing the circumstances to and obtaining the approval of his employer.

2. That an employee is not to engage in any transaction for personal profit with a customer of the employer with whom the employee deals, without the employer's knowledge and consent.

3. That an employee is not to engage in any business activity which conflicts with or may be detrimental to the employer's interest, without the employer's knowledge and consent.

4. That an employee is not to conceal or withold information, such as a borrower's true financial status or ability to repay money loaned, which information is necessary to the employer's competently and intelligently evaluating his business risks.

5. That an employee is not to acquire or maintain any ownership interest in the business of a customer

or the employer with whom the employee deals without his employer's knowledge and consent.

6. That an employee is not to borrow money from his employer without the employer's knowledge and consent.

7. That an employee is not to release collateral securing a loan made by the employer which increases the business risks of his employer without the employer's knowledge and consent.

8. That an employee is to take adequate security for loans made by or on behalf of the employer which the known facts indicate require such security unless the employer with full knowledge of the facts and circumstances consents otherwise.

9. That the employee so far as possible shall follow the employer's instructions as to all things pertaining to the relationship.

A breach of one or all of the foregoing duties does not necessarily in and of itself indicate that there was any fraud or dishonesty with respect to the plaintiff's contentions. In fact, mere breach of duty without fraud or dishonesty, as I have heretofore defined those terms, is not a sufficient basis upon which you can find for the plaintiff or answer an interrogatory in the affirmative. However, you may consider such breach, if any, in determining whether any one or more of the principals acted fraudu-

lently or dishonestly, keeping in mind, however, that the plaintiff must prove its contentions to you by a fair preponderance of the evidence.

The plaintiff contends and the defendant concedes that there was a lack of good faith on the part of the principal John Koster in his signing the name of John Kiltheau to a check made payable to said Kiltheau in the amount of $425.00. You may only consider this, however, together with all other evidence in the case, for the purpose of determining whether John Koster acted fraudulently or dishonestly, with respect to the plaintiff, as I have defined those terms, keeping in mind that the plaintiff must prove its contentions to you by a fair preponderance of the evidence.

While the law will not presume fraud or dishonesty nor infer it merely because loans made by an employee of his employer's funds were irregular, unsafe or unsound, such factors may nevertheless be considered by you together with all of the evidence to aid in the correct determination of whether fraud or dishonesty was, in fact, involved in any of the transactions contended by the plaintiff to have been fraudulent or dishonest.

If any one of the principals is found from a fair preponderance of the evidence to have made or caused to be made any dishonest or fraudulent loan to a borrower or borrowers, then it would be immaterial that any such prin-

cipal, at the time of making any such fraudulent or dishonest loan, may have hoped or expected that the particular borrower might ultimately repay such loan or loans.

None of the evidence presented during the trial of this case concerning the Cabadab transaction or the Radio Station KYSS transaction shall be considered in your deliberations in this case.